

# Operationalising Financing Windows for Entrepreneurship Development in Nigeria: An Appraisal

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## ABSTRACT

Entrepreneurship has been seen as a linchpin for economic development, employment generation, citizen empowerment and wealth creation all over the world. More importantly, entrepreneurship development has been conceived as an instrument to suppress major avatars of poverty and socioeconomic deprivations among Nigerian citizens and for engendering social cohesion. However, harnessing the foregoing benefits has been hamstrung by lack of access to or inadequate supply of entrepreneurial finance. In addition to blistering ecological forces such as spotty power supply, an inept and unorganised political leadership that is irresponsible and unresponsive to the plight of the people, polygonal political corruption, putrefied or inadequate basic infrastructure like roads, among others, lack of SME finance has remained a minatory albatross to entrepreneurship development in the country. This paper, therefore, examined extant SME funding windows in Nigeria, identified their challenges and proffered solutions, while generally suggesting ways to operationalise both existing and neoteric funding options to enable entrepreneurship development happen in Nigeria.

**Keywords:** Operationalising; Entrepreneurship Development; Entrepreneurial Finance; SMEs; Ecological Forces.

## Introduction

Entrepreneurship has become the new bride courted by developing, developed and post-industrial societies because of its endogenous dynamics which are capable of stimulating employment for citizens, spawning micro, small and medium enterprises (MSMEs), triggering innovations, providing essential products and services, supporting the value chains and alleviating extreme and other avatars of poverty and socioeconomic deprivations. OECD (2012) particularly describes SMEs, creations of entrepreneurial exertions, as important engines of growth, jobs and social cohesion. Thus, numerous scholars and writers consent to the view that entrepreneurship in itself is the engine of economic growth and industrial development in all societies (Adewale, 2005; Ewiwile, Azu & Owa, 2011; Imhonopi & Urim, 2012; Imhonopi, Urim & Ajayi, 2013; Kerr & Nanda, 2009). Commenting on the debouchment of SMEs in Nigeria, a product of entrepreneurial activities, Adewale (2005) contends that the former are particularly suitable for the diffusion of management skills, fostering and stimulating of indigenous entrepreneurship and are economic engine of growth within the country. Therefore, there is a push for entrepreneurship development at all levels of government in Nigeria as a way of generating employment opportunities, engaging the distended army of youth and the vulnerable sector and improving the personal economies of citizens (Imhonopi & Urim, 2012).

Nevertheless, in spite of this promissory intrinsic worth of entrepreneurship, there is unanimity of views that there are conundrums within the entrepreneurship ecosystem that throttle its development. The business ecology, according to some authors, for instance, plays a fundamental role in encouraging or limiting entrepreneurial success within a national locale (Abimbola & Agboola, 2011; Borkowski & Kulzick, 2006; Carter & Wilton, 2006). This is patent in a developing economy like Nigeria, where blistering ecological forces exist such as spotty power supply, an inept and unorganised political leadership that is irresponsible and unresponsive to the plight of the people, polygonal political corruption, putrefied or inadequate basic infrastructure like roads, healthcare and water, lack of capacity building opportunities for entrepreneurs, an adversarial business environment with visible problems (for example, double or triple taxation, rigid and problematic business registration processes, limited access to and expensive price of land for manufacturing or agricultural purposes) and lack of access to finance. Of all the items on this list, finance has been seen as a major constraint on entrepreneurship development in Africa, including Nigeria (Imhonopi *et. al.*, 2013; Miasamari, 2011; OECD, 2012). In fact, the importance of SME finance is now widely recognised. According to a report, at the Pittsburgh Summit in 2009, G20 Leaders acknowledged that access to finance provides growth opportunities for businesses and the economy as a whole (OECD, 2012). The report also identified Financial Inclusion as a pillar of the G20 Multi-Year Action Plan on Development, and this was given teeth with the launch of the G20 Global Platform for Financial Inclusion (GPFI) in Korea in December 2010. The report added that the need to address the financing hurdles to SME growth was also underlined by G8 Leaders at the 2011 Deauville Summit, where the OECD was invited, in co-operation with other relevant international institutions, to identify impediments to SME growth, including the issue of private funding.

Since access to finance is important to all enterprises regardless of their size, it means that when it is inaccessible or inadequate, entrepreneurship will suffer numerous backflips in its growth trajectory; employment

generation will be stifled and economic development will be negatively affected. Thus many scholars are of the opinion that unless the financial markets are liberalised and innovative funding windows are created to underprop entrepreneurial activities in the society, including Nigeria, the underlying benefits entrepreneurship development portends may not be realised within the society (Denis, 2004; Garba, 2005; Imhonopi *et. al.*, 2013; Kerr & Nanda, 2009; Zavatta, 2008). While arguing that supply and access to capital are critical to stimulating entrepreneurship and economic growth, another recent report observed that up to 84% of small and medium-sized enterprises (SMEs) in Africa are either un-served or underserved, representing a value gap in credit financing of up to USD 140-170 billion (Omidyar Network Africa, 2012). This blights entrepreneurship growth and development in many African countries, including Nigeria, leaving many of the populations on the fringes of poverty, economic marginalisation, unemployment and frustration. This has reproduced a growing class of precariat; what Standing (2011) has styled the new dangerous class, which has become a cannon fodder for all social convolutions in many parts of the world including Nigeria (Imhonopi & Urim, 2013). This paper seeks to operationalise financing windows, including neoteric options, for entrepreneurship development in Nigeria.

### Conceptual and Theoretical Framework

According to Sethi (2013), entrepreneurship is a process or action undertaken by an entrepreneur to establish an enterprise. It involves a creative activity or process which could involve building a social or economic entity from practically nothing or sensing an opportunity where others see chaos, contradiction and confusion and exploiting it. Sethi adds that entrepreneurship also includes the attitude of mind to seek opportunities, take calculated risks and derive benefits by setting up a venture comprising numerous activities involved in the conception, creation and running of an enterprise. It could also refer to the pursuit of an opportunity beyond resources controlled (Stevenson, 2013). According to Zimmerer and Scarborough (2006), although the creation of business is certainly an important facet of entrepreneurship, it is not the complete picture. The characteristics of seeking opportunities, taking risks beyond security and having the tenacity to push an idea through to reality combine into special perspectives that depict entrepreneurs. Hisrich and Peters (2002) posit that entrepreneurship is the process of creating something new with value by devoting the necessary time and effort, assuming the accompanying financial, psychic and social risks and receiving the resulting rewards of monetary and personal satisfaction and independence. Potekar (2009) observes that entrepreneurship is the practice of starting new businesses or revitalising matured organisations, particularly new businesses generally in response to identified opportunities. In their attempt to distinguish the differences that exist between SMEs and entrepreneurship, Lucky & Olusegun (2012) argue that while entrepreneurship is the process of nurturing the entrepreneur to recognise opportunities in the environment so as to mobilise resources, by taking risk in order to create wealth and at the same time make profit through effective and efficient management of an entity (business), SMEs are products of entrepreneurial activities. Putting this differently, while entrepreneurship is seen as the process and the entrepreneur the actor, the small and medium enterprise (SME) or company created is seen as the outcome of the entrepreneurial process.

On the other hand, entrepreneurial finance refers to that multi-layered funding spectrum, including formal and informal funding windows, available to and accessible by the entrepreneur. However, it has been abstracted as that type of funding provided to high-risk, high-potential entrepreneurial projects, usually by venture capitalists or business angels in exchange for equity (Cippolone & Giordani, 2012). These scholars see this model of financing innovation as relatively novel and that it stands in contrast with the alternative, more traditional, bank funding paradigm (what they call corporate R & D model). This abstraction is obviously inadequate because it fails to capture the different financing dynamics open to the entrepreneur. In contrast, this paper sees entrepreneurial finance, or what is sometimes termed SME finance, as the eclectic financing windows comprising equity to debt-related financing opportunities or both (whether formal or informal) accessible by start-ups as well as growing and established businesses and provided by institutional and non-institutional vendors (Imhonopi, Urim, Suleiman & Amusan, 2013).

The Theory of Financial Intermediary has been adopted in this work. This theory seeks to explain the behaviour of financial intermediaries in their relation to savers and to investors or entrepreneurs. Borrowing from the famous classical idea of the perfect market, introduced by Marshall and Walras, the Theory of Financial Intermediary is claimed to have become the leading quality check used in many economic theories (Scholtens & van Wensveen, 2003). This theory posits that financial intermediaries have a function to discharge to entrepreneurs only because financial markets are not perfect (Imhonopi, *et. al.*, 2013). In other words, market imperfections make financial intermediaries relevant in providing financial services to entrepreneurs and/or investors. Thus, financial intermediaries play an important role in deciding which projects to fund and monitor after funding. Kerr & Nanda (2009) argue that as the costs of acquiring information about borrowers increase, it becomes harder to fund them profitably. This is where established firms have several advantages because of their possession of audited financial statements, adequate collateral to pledge against loans, and potentially the ability to partially fund expansion through retained earnings. On the other hand, information asymmetry and limited

assets are particularly acute for potential entrepreneurs, resulting in good projects going unfunded because intermediaries are unable to evaluate them effectively. However, financial intermediaries may cease to function when savers and investors/entrepreneurs have the perfect information needed to find each other directly, immediately and without any impediments or costs, and are able to deal with one another at optimal prices. According to Arrow & Debreu (1954), the following criteria typify a perfect market:

- no individual party on the market can influence prices;
- conditions for borrowing/lending are equal for all parties under equal circumstances;
- there are no discriminatory taxes;
- there is absence of scale and scope economies;
- all financial products are homogeneous, divisible and tradable;
- there are no information costs, no transaction costs and no insolvency costs;
- all market parties have *ex ante* and *ex post* immediate and full information on all factors and events relevant for the (future) value of traded financial instruments.

The Arrow-Debreu model is based on the intellection of complete markets where present value of investments is well defined, and savers and investors or entrepreneurs find each other because they have perfect information on each others' preferences at no cost in order to exchange savings or idle funds in favour of preferred investments. However, since this utopia does not exist naturally, intermediaries are useful to bring savers and investors together and to create instruments that meet their needs. They do so in expectation of the reimbursement of costs. Therefore, intermediaries are at best tolerated and can only be eliminated when market perfection is reached, creating a perfect state of disintermediation. However, as Scholtens & van Wensveen, (2003) observed, increasing liberalisation and deregulation of financial markets and the rise of a sextet of ICTs, suggest that information on important macroeconomic and monetary data and on the quality and activities of market players will be available in 'real time', on a global scale, twenty-four hours a day. This means that firms that issue shares over the Internet and investors can put their order directly in financial markets due to the virtual market without the need for intermediation. The ICT revolution also reduces information costs tremendously. Meanwhile, the liberalisation and deregulation of financial markets create the appearance of transparent, homogeneous, and tradable investment instruments in the international financial centres in the world. Only taxes are discriminating, inside and between countries. While, transaction costs are still there, they are declining in relative importance as a result of the cost efficiency of ICT and efficiencies of scale (Scholtens & van Wensveen, 2003).

While this order may be visible in the financial markets of developed societies, in Nigeria with diverse development challenges such as a bloated informal sector, infrastructural deficiencies, information asymmetries, an inchoate financial services sector, multiple tax regimes and other features that describe an imperfect market, financial intermediaries like banks, microfinance institutions, development institutions, thrift cooperative societies, venture capitalists, angel investors and their ilk, have a role to play in providing financial services/products needed by entrepreneurs to start, grow or expand their businesses within a wide continuum of very formal to informal processes in accessing required funding (Imhonopi, *et. al.*, 2013). The only sore point is that commercial banks in Nigeria, for instance, have been known to be favourably disposed to established entrepreneurs who possess good cash flow history, collaterals, and established financial management processes, among others, than SMEs who are mostly seen as high-risk businesses with no credit history, liquid or physical assets or audited financial accounts. These factors do immobilise entrepreneurs when they seek equity or debt funding as financial intermediaries prefer to advance such facilities to more established businesses. Therefore, expanding the present bandwidth of entrepreneurial funding windows, including reproducing neoteric options, could help in fostering entrepreneurial development in Nigeria, as well as in the global south.

### **Extant Financing Windows for Entrepreneurship Development in Nigeria and their Challenges**

This section has grouped extant funding windows for entrepreneurship into two:

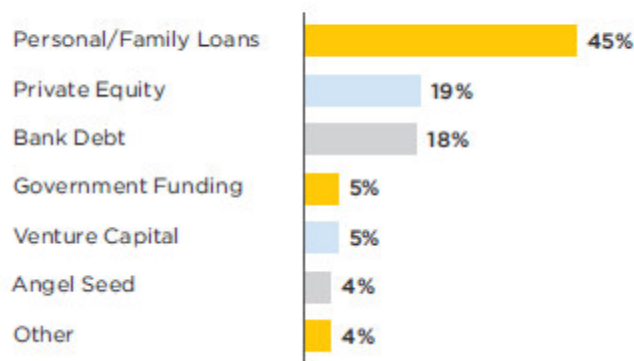
1. Non-State Funding Windows for Entrepreneurship
2. Government-Based Funding Initiatives for Entrepreneurship

#### **Non-State Funding Windows for Entrepreneurship**

Existing non-state or non-governmental funding windows for entrepreneurship development in Nigeria include both internal and external funding sources. Concerning internal funding windows for entrepreneurship development in Nigeria, literature is replete with self-finance and informal sources as the main sources of finance used by most entrepreneurs in Nigeria. According to Ewiwile, Azu & Owa (2011), many entrepreneurs within the small-scale business ecosystem depend on personal savings, borrowings from friends, relatives and business partners to start or grow their businesses. This view is consistent with the findings by the OECD (2006) that the seed money to start up entrepreneurial ventures generally comes from friends, professional contacts and family. In a recent study on *Accelerating Entrepreneurship in Africa Initiative* in 2012, involving a survey of 582

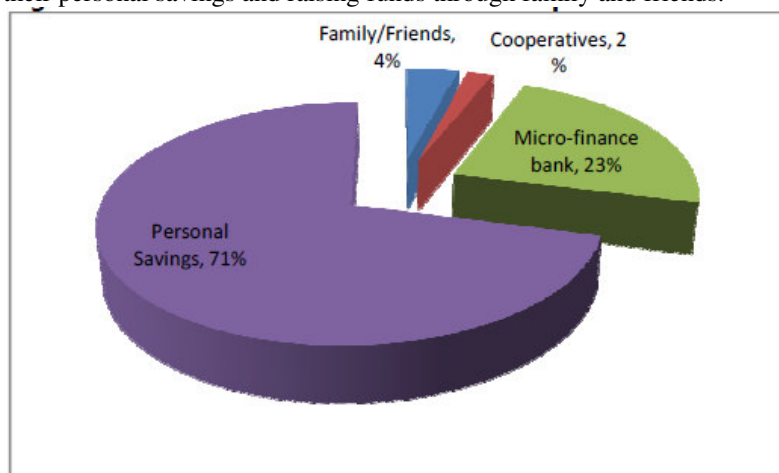
entrepreneurs and 72 in-depth interviews conducted in six sub-Saharan African countries, namely, Ethiopia, Ghana, Kenya, Nigeria, South Africa and Tanzania, findings revealed, as illustrated in the figure below, that self-finance and family loans are the main sources of funding for entrepreneurs in the selected African countries.

#### Self Finance and Family Loans are the Main Sources of Funding



Source: Omidyar Network Africa (2012).

The above finding is consistent with an earlier study carried out by Abiola & Salami (2011) among some micro-entrepreneurs in Oyo state, Nigeria, in which most respondents claimed they started their businesses by using their personal savings and raising funds through family and friends.



Source: Abiola & Salami (2011).

Garba (2005) adds that beyond personal savings and family grants that entrepreneurs receive to start their business ventures, other internal funding sources open to entrepreneurs include retained earnings from the business which are ploughed back into it, sale of assets to raise money and use of the depreciation reserve. Generally, this informal and internal financing vehicle is advantageous to entrepreneurs because it puts less pressure on them even if the business fails and in most instances, there is no commitment of repayment on the part of the entrepreneur; even when the repayment process is in place, it is mostly relaxed. Cornwall, Vang & Hartman (2009) call this form of financing “bootstrapping” which is the use of limited resources available to most start-up ventures to find creative ways to exploit opportunities for launching and growing their businesses. According to Cornwall (2009), even when some new ventures fit the criteria for external debt or equity investment, they may still choose to minimise the use of outside funding or delay its use for as long as possible, a proceeding commonly known as “extending the runway” (Berkus, 2006). Cornwall (2009) reasons that by postponing outside funding, more value is created in the business due to its larger size and established cash flow. This puts the entrepreneur in a stronger bargaining position with external funders and gives the entrepreneur more time to set the vision and culture of the business without having to navigate and integrate the potentially varied aspirations of external financiers. Sometimes, entrepreneurs continue to bootstrap even beyond the start-up period of their business because this tactic helps them to reduce the risk the business might face during difficult economic times when sales may be soft, when inflation heats up or when interest rates climb (Cornwall, 2009). The internal sources for entrepreneurial finance are also called the traditional sources. However,



challenges facing internal funding windows include (i) the present cash squeeze felt by citizens as a result of the global financial meltdown; (ii) the general economic downturn which has forced most people to adopt austere measures in the management and distribution of their resources; (iii) the macroeconomic situation of the country which acts as a scarecrow for entrepreneurial activities and demotivates family and friends from committing their hard-earned resources to such ventures and (iv) the inadequacy of this form of financing for entrepreneurs especially when they want to scale up their business operations.

The entire kaleidoscope of external funding for entrepreneurs in Nigeria include credit and thrift societies, commercial banks, business angels, venture capitalists, development finance institutions and government-sponsored credit and loan schemes and programmes. The latter, which are government-crafted funding windows for entrepreneurial ventures in Nigeria will be treated separately under the section on government-based funding. The need for external funding is accentuated during the growing stages of an enterprise. As SMEs begin to grow, but have yet to establish the track record or size and collateral that would give them access to bank financing, they tend to turn to other types of risk capital offered by venture capitalists, who favour larger projects at later stages of the business cycle and/or business angels who support start-up projects. Furthermore, funds are usually obtained from institutional investors, especially pension funds, but financial intermediaries and the corporate sector are also major investors (OECD, 2006). According to Garba (2005), entrepreneurs resort to external funding vehicles when internal sources of financing are inadequate and they fail to meet the expansion or growth plans of the firm. He divided these sources into short and long-term sources. The short-term sources include: (i) cash deposit from customers for the supply of goods or services at a future date; (ii) trade credit which allows entrepreneurs to make payment for goods supplied at a later date; (iii) equipment leasing which allows entrepreneurs to possess a piece of equipment for a specific period in return for payment (iv) hire purchase which allows entrepreneurs to take possession of an expensive piece of equipment/property while making regular payments on it, with legal ownership transferred only after it is fully paid for; and (v) commercial bank loans which are given at high costs of the funds which make them an unsustainable form of borrowing for many entrepreneurs. He considers the long-term external funding vehicles as (i) debentures which are corporate loans given to borrowers and that small enterprises might not likely qualify for (ii) preference shares which are debt instruments where the lenders are both equity and debt holders to the firm (iii) ordinary shares which are equity holders in the firm and are the real risk bearers (iv) development banks such as the Bank of Industry and the Nigerian Agricultural Credit and Rural Development Bank (NACRDB) which service the funding needs of enterprises and (v) Esusu which is a cooperative-based thrift collection affording members to pool their resources together, with each member collecting the total sum contributed per time in turns until the cycle is completed. The challenges with accessing short-term external funds include (i) the cost of funds may be expensive (ii) the perception of entrepreneurial ventures as high-risk businesses work against them (iii) customers may not want to make cash deposits to firms they consider newbies in the market (iv) cash instalments for hire purchase contracts and equipment leases may be expensive when added up. Challenges of accessing long-term external funds include (i) regulatory hurdles which may debar SMEs from being registered on the local stock exchange (ii) finding an investor whose terms and demands will be acceptable to the borrower's short- and long-term plans could prove difficult, if not herculean (iii) the perception that entrepreneurial ventures are high-risk borrowers due to insufficient assets and low capitalisation, vulnerability to market fluctuations and high mortality rates (iv) the existence of information asymmetry in the areas of absence of accounting records, inadequate financial statements or business plans makes it difficult for creditors and investors to assess the creditworthiness of potential SME proposals (v) and importantly, high administrative/transaction costs of lending or investing small amounts in SMEs make it unattractive to institutional lenders. The conflation of these factors, among others, makes entrepreneurial financing appear to be an unprofitable business.

### **Government-Based Funding Initiatives for Entrepreneurship Development in Nigeria**

Globally, many more governments are recognising that entrepreneurship can be a huge contributor to economic growth and are beginning to support efforts and initiatives that encourage innovation and enterprise-creation. Successive Nigerian governments, over the years, have been seen to show much interest in and passion for the growth and development of the SME sector through entrepreneurial activities. The dip in the fortunes of the state starting from the 1980s further increased the frenzy in government quarters in the area of SME finance. The following is a brief chronicle of the various measures put in place and institutions established by the Nigerian government over the years to support entrepreneurship development and to transform the economy from its rudimentary state to a highly industrialised one. According to Imhonopi *et. al.*, (2013), recognising the role of credit as an essential intermediary for the promotion of entrepreneurship development, government's first effort to underprop the entrepreneurial sector was to establish a credit scheme administered by state and federal governments to liberalise the economy through the Ministry of Commerce and Industry, and the National Agricultural and Cooperative Bank (NACB). Government also made concerted efforts to revamp the economy

by having a redirected focus towards business in various dimensions such as the Green Revolution, Operation Feed the Nation, National Directorate of Employment (NDE), Family Economic Advancement Programme (FEAP), Poverty Alleviation Programme, Nigerian Agricultural and Co-operative Bank (NACB), Nigerian Industrial Development Bank (NIDB), the Nigerian Bank for Commerce and Industry, Equity Investment Scheme, among others. Imhonopi *et al.*, (2013) noted that the Development Finance Institutions/Banks (DFIs) that were established had a three-tier structure in the country. The first-tier included the National Development Banks i.e. the NACB, NIDB, Urban Development Bank, NBCI and the Nigerian Export-Import Bank. The second-tier consisted of Inter-State DFIs i.e. the O'dua Investment Limited and the New Nigeria Development Company Limited (NNDC). The third-tier consists of state-owned DFIs i.e. the Kwara State Property and Investment Company and the Oyo State Agricultural Development Programme (OYSADP). Thus, apart from conventional banks (commercial and merchant), government established these Development Finance Institutions and Credit Schemes to assist entrepreneurship development in Nigeria: (i) Nigeria Industrial Development Bank (NIDB); (ii) Nigeria Bank for Commerce and Industry (NBCI); (iii) World Bank Assisted SME Loan Scheme; (iv) Nigerian Agricultural and Co-operative Bank (NACB); (v) Federal Ministry of Commerce and Industry's Small-Scale Industries Credit Scheme; (vi) Community Banks that later transitioned to Microfinance Banks; and (vii) the National Economic Reconstruction Fund (NERFUND). Much later, in order to strengthen the functions of these institutions and to reduce operating costs, government merged the Nigerian Industrial Development Bank (NIDB), the National Economic Reconstruction Fund (NERFUND) and the Nigerian Bank for Commerce and Industry (NBIC) to form the Bank of Industry (BOI) while the Family Economic Advancement Programme (FEAP), Peoples Bank of Nigeria (PBN) and the Nigerian Agricultural and Cooperative Bank (NACB) were also merged to become a single bank, i.e. the Nigerian Agricultural, Cooperative and Rural Development Bank (NACRDB).

Government also tasked commercial banks to provide schemes and financial products to meet the needs of entrepreneurs in the country. One of such schemes was the Small and Medium Enterprises Equity Investment Scheme (SMEEIS) which was believed to have the potential to trigger a turnaround in the entrepreneurial sector. The SMEEIS was initiated by the Bankers' Committee and became operational in 2001. The scheme required all banks to set aside ten percent of their annual after-tax profits for investment in SMEs. These could take the form of loans or equity, although a mandated 9% interest rate cap on loans reduced incentives to lend and led banks to seek equity investments in SMEs. SME equity investments which are generally quite problematic, given due diligence requirements and difficulties in exiting the investments through the sale of shares also surfaced in the SMEEIS Scheme and were further compounded by the banks having little experience in identifying suitable SMEs. As Fuchs & Radwan (2009) noted, as at the end of December 2008, SMEEIS investments totalled ₦28 billion (US\$ 194.4 million) in 333 companies, out of a total of ₦42 billion (US\$ 291.6 million) in the SMEEIS fund. In an attempt to enhance the performance of the scheme, some banks decided to establish specialised venture capital companies with the Securities and Exchange Commission (SEC) to manage the funds. Although in early 2008, the low level of funds invested and changing national priorities led the Bankers Committee to discontinue SMEEIS and transfer the balance to a Microcredit Fund; most of the newly created venture capital funds are still in operation nonetheless. The lessons learnt from this experience could prove useful for banks aiming to target SME investments and there is evidence of more banks beginning to offer better tailored services to SMEs building on this venture capital fund experience such as Diamond Bank, former Oceanic Bank and Ecobank. Microfinance banks, some of whom were defunct community banks, were also registered to provide micro-credit and loans to micro and small entrepreneurs but their impact on the entrepreneurial sector is yet to be felt in the country because of the inclement macroeconomic business environment and the high operating costs facing businesses generally in the country.

### **Operationalising Financing Windows for Entrepreneurship Development in Nigeria**

As Sutton & Jenkins (2007) contend, financial services are fundamental to economic growth and development. Consequently, banking, savings and investment, insurance, debt and equity financing help private citizens save money, guard against insecurity and build credit, while enabling businesses to start up, expand, increase efficiency, and compete in local and international markets. Entrepreneurial firms have been adjudged to play a frontline role in modern economies. As Sanders & Wegener (2006) observed, in many developing countries, SMEs with fewer than 50 employees constitute 95% of all businesses. And yet, SMEs in developing countries contribute far less to GDP and employment than their developed counterparts: 17% and 30%, respectively, compared with 50% and 60% in developed countries. As part of the reasons for this overcast situation, in their study of entrepreneurship problems in Nigeria in comparison with Sweden, Eriobunah & Nosakhare (2012) found out that while finance was the least problem facing Swedish firms, it was the major cause of insomnia for Nigerian entrepreneurs. This view had been underscored by Akingunola (2011) who argued that lack of access to credit facilities or funding windows was the principal reason for the inability of SMEs to meet the expectations of government in accelerating job creation, increasing the production of goods and services, facilitating

technology transfer, creating more opportunities for entrepreneurs and, in particular, increasing the local content job and service components required by multinational firms in Nigeria. Thus, this paper advocates for the operationalisation of some financing windows in Nigeria with the goal to strengthen the SME finance ecosystem in the country, thus providing a robust ecology for entrepreneurship development. Some of these funding vehicles have been identified below.

### **1. Venture Capitalists (VCs)**

Venture capitalist companies are professionally managed pools of capital (whether private or publicly sponsored) that take an equity position in rapidly growing private companies. The costs of evaluation and monitoring militate against smaller venture capital investments, because investments are typically not less than \$1 million USD. Until recently, only the United States had an active venture capital market, but these days many countries have experienced rapid growth in venture capital financing since the mid-1990s. Venture capitalists are interested in investing in those rare companies with the potential of going public or being acquired at a premium within a few years and that offered investment returns of 25–50 percent per year. Venture Capitalist firms have been in operation in Nigeria for a while. However, since many of these VCs are offshoots of commercial banks, their operational template derives heavily from that of their parent companies, hence they replicate the same fundamental errors inherent in banks' funding experience with entrepreneurial firms. While this is not enough to discard the idea of funding entrepreneurial firms in Nigeria through well-established VCs, it is important that the existing operational templates of these VCs be changed to reflect the unique funding needs and aspirations of entrepreneurial firms. To encourage more VCs to put up a strong presence in the SME finance ecosystem in Nigeria, there is need for government to evolve a friendly regulatory environment that would apply more flexible and clement tax and subsidy measures to the capital gains and profits these firms will be making, and also creating more exit options for them to recoup their investments so they can be committed to playing their role in revamping the entrepreneurship sector in the country.

### **2. Angel investors or business angels**

Business Angels or angel investors, also known as informal or private investors, are prototypically wealthy individuals who invest directly in small firms owned by others in exchange for convertible debt or ownership equity. Though largely invisible, informal investment is a significant source of financing for early-stage enterprises. Estimates of the rate at which angels invest range from two to four times the rate at which institutional venture capitalists invest in early-stage businesses. However, informal angel investments tend to be small in scale and complementary to financing provided by institutional venture capital companies. Angels provide early start-up money and things like networks, mentoring and other contacts. This is why angel investment is called *mentor or patient financing*. However, angels and VCs share the following crucial feature: they are expected to contribute not only financial investments but also managerial and technical expertise to entrepreneurial firms. Like it should do to VCs, government needs to incentivise local angel investing ecosystems in the country by way of tax deductions and/or exemptions, or low subsidies and even provide them with national honours as a way of inspiring them to commit their resources to helping young entrepreneurial firms find their feet in the marketplace.

### **3. Business incubators**

Incubators and accelerators, though in their infancy, in many parts of Africa can offer entrepreneurs vital support during the start-up phase. To be effective, incubators must focus on a limited number of entrepreneurial firms to provide with a high-level support that entrepreneurs need to launch, find and serve new customers and scale. Against the backdrop of the lack of entrepreneurship training in African schools, a trend that is being reversed through the introduction of entrepreneurial studies in the educational curriculum across board, as is being witnessed in Nigeria, incubators can help in closing the gap in entrepreneurial capacity building. Incubators can provide such services as physical incubation (setting up of offices and structures required to function), build networks of advisory-service providers and create funding windows. The Nigerian government can collaborate with the private sector to set up business incubators for entrepreneurial firms so that entrepreneurship development can crystallise in the country.

### **4. Corporate investors**

There are non-banking corporations that may be interested in funding entrepreneurial projects either as part of their backward or forward integration or value chain or as part of their corporate social responsibility. Such firms should be encouraged and provided with incentives. These could include tax rebates, government subsidies and other opportunities. Such companies should also be given preferential access to government business opportunities.

## **5. Initial Public Offering (IPO)**

An IPO is the process whereby a firm sells equity to the public for the first time, usually by issuing shares through investment dealers. IPO's are an important element in the market for capital. They provide the exit that allows early-stage investors, venture capitalists, merchant bankers, and owners to exit the firm and realise a return on their early-stage investments. An efficient IPO mechanism offers the prospect of a profitable exit for early-stage investors and therefore encourages risk taking. IPOs are also a means by which the firm can raise the significant amounts of capital often required to support substantive growth steps. The Nigerian Stock Exchange, the Security and Exchange Commission and other regulatory bodies and the government should make the conditionalities for registration on the stock exchange flexible for SMEs so they can become eligible.

## **6. New national loan guarantee scheme**

There is need to evolve a feasible loan guarantee scheme in collaboration with commercial or development finance institutions as part of government's effort to create funding opportunities for entrepreneurial firms.

## **7. New seed enterprise investment**

This investment should be modelled to target start-up firms who need seed funds to build their project or product prototypes, carry out feasibility studies or as part of their start-up funds. To achieve its sustainability, the investment should be professionally managed preferably under a public-private partnership.

## **8. SME Equity Bank**

The existing development finance institutions have been unable to create an attractive SME finance ecosystem favourably disposed to entrepreneurial firms. Therefore, evolving an SME Equity Bank, either government sponsored or government-private sector sponsored, will help to liberalise greater SME access to funding opportunities. This bank should cater for pre-seed, seed and start-up needs of SMEs since many institutional investors will prefer to invest in growing and established firms.

## **Conclusion and Recommendations**

The Nigerian government, like other African governments, over the years, has increased support for entrepreneurs by creating several initiatives to encourage entrepreneurship development. However, the results of these initiatives have been limited. According to a report, many large government-assistance programmes for SMEs in Africa, including Nigeria, have not worked for two reasons: (i) mass scale orientation of factory-like business assistance which kept to a one-size-fits all template instead of a bespoke approach; (ii) lack of requisite motivation and skills by government personnel to assist entrepreneurs since entrepreneurs are best assisted either by other entrepreneurs or by established functional or industry experts who possess appropriate and relevant expertise (Omidyar Network Africa, 2012). According to Imhonopi *et al.*, (2013), other reasons for the failure of government-sponsored entrepreneurial financing windows include banks' risk aversion in lending to entrepreneurial firms; (ii) Stiff collateral demands and high interest rates; (iii) Limited managerial capability of entrepreneurial firms due to inexperience, illiteracy and absence of mentoring and entrepreneurial network; (iv) Politicisation of resources and benefits by many of the public-owned DFIs; (v) Lack of policy stability; (vi) Lack of political will and sincerity on the part of government and its private-sector allies; (vii) Absence of an enabling business environment for the private sector, grass-root organisations and cooperatives or self-help groups to effectively engage in entrepreneurial activities; (viii) Lack of a good framework for monitoring, implementing, and evaluating performance of entrepreneurial firms and inimical monetary and fiscal policies which are anti-entrepreneurship development; (ix) and unfavourable legal and regulatory policies such as building codes and zoning regulations which pose enormous difficulties for entrepreneurial firms that find the high costs of compliance, both in time and monetary terms unaffordable.

**Therefore, operationalising neoteric funding vehicles and improving existing provisions by addressing inherent weaknesses will spur entrepreneurship development in Nigeria. The following provisions could further these objectives:**

Government should reduce the red tape for early-stage companies to access government funding in order to provide 'softer' sources of financing for newbie entrepreneurs. Government should expand/initiate local angel investing ecosystems to ensure the availability of the most appropriate type of funding for start-ups, especially for entrepreneurs who lack the network of friends and family that traditionally play this role. As a corollary, tax and other incentives should be provided to formal, as well as informal (including friends and family), angel



investors to make it easier for people who have extra cash to invest in start-up businesses and reduce their risk. Tax and other incentives should also be given to large clients of early-stage ventures to provide supplier credit to incentivise and reduce the risks suppliers face when providing generous payment terms and/or stock to new ventures. The creation of an SME Equity Bank could further help to increase entrepreneurial firms to access cheap funds for their start-up ventures. Government and its private sector allies should strive to close the information gap regarding entrepreneurs' knowledge about possible sources of funding outside banking systems. Government can leverage indirect personal sources of funding, such as pension funds to finance SME operations, so that more resources are available to fund more-established enterprises where the risks are lower. Government should also expand or initiate local venture capital investing ecosystems to ensure that the most appropriate source of funding is available for companies at the mid-level stage of development. Typically, mid-sized companies need banking overdraft facilities to cover predictable working capital and debt to finance certain types of capital investments and second rounds of equity to finance expansions. This kind of funding can be made available through venture capital firms and possibly private equity funds for the larger mid-sized companies. Local banking systems can be used to disburse donor or government lines of credit to SMEs to reduce prohibitive interest rates and collateral requirements. This approach puts enterprise funding in the hands of commercial bankers who are trained to assess risk and evaluate potential clients but may lack the kinds of 'soft funds' needed to take slightly less-secured credit-equity positions. Government should provide incentives and support to mid-sized SMEs to practise sound financial management and maintain adequate records, including audited statements. This will make enterprises more fundable as investors will invariably ask for reliable financial information. Government should also create a greater fenestra for capital-raising engagement programmes by linking well-established private-owned enterprises with entrepreneurs who are desirous of benefitting from private equity funding, as well as the benefits of being listed on the local stock exchange. Through this process, exit options will be created for institutional VCs and investors who may like to exit after early-investment is done. The Nigerian government can also work with other African nations to create SME finance windows, encouraging debt and equity financing for the nation's businesses looking to expand across the continent.

The Nigerian government cannot afford to toy or play politics with its entrepreneurial sector because of the endogenous advantages the latter has in the area of employment generation, economic empowerment and other promissory benefits. Consequently, operationalising neoteric SME funding windows and removing identified obstacles embedded within existing SME funding ecosystems will guarantee the robustness and resilience of the entrepreneurial sector to meet the yearnings of the people and government of Nigeria for development, while creating the right climate for entrepreneurship development to thrive.

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